

ADMINISTRATIVE - INTERNAL USE ONLY

DD/S 68-5750

27 NOV 1968

**MEMORANDUM FOR: Executive Director-Comptroller**

**THROUGH : Deputy Director for Support**

**SUBJECT : Voluntary Employee Savings and Investment Plan of  
the Tennessee Valley Authority (TVA)**

1. The TVA voluntary employee savings and investment plan is known as the Take Stock Plan and will generally be identified by this name in this report. The plan is fully and succinctly described in the brochure attached at Tab A. It is suggested that the brochure be read before continuing in this report.

2. Attention is called immediately to the fact that the Take Stock Plan is not merely a means by which TVA employees can conveniently through payroll deductions and TVA-provided administrative support pool their savings and effect substantial economies on sales commissions in the purchase of "load" mutual fund shares. Rather the TVA has contrived and fostered the Take Stock Plan as an integral part of its employee retirement program so that the Take Stock Plan will qualify with the Internal Revenue Service as a trust under Section 401(a) of the Internal Revenue Code and acquire exemption from income taxes under the provisions of Section 501(a). As a qualified voluntary retirement plan, no income taxes are payable on interest, dividends, or capital gains realized on invested employee savings until the individual retires (or withdraws his funds). At such time, any appreciation or increase in the value of the individual's shares in the investment fund are taxable solely as long term capital gains. Since this usually occurs at a period in life when the individual's taxable income is greatly reduced, taxes paid are unusually low. In addition to this significant advantage, there is the additional advantage that all earnings and gains are automatically reinvested without annual income tax dilution, resulting in a significantly larger investment base for further earnings and appreciation.

3. Basic to any consideration of a proposal to establish a voluntary employee retirement trust with its attendant costs and administrative responsibility is the rationale or *raison d'être* for doing so. The TVA believes that educating, encouraging, and assisting employees to make adequate financial preparation for retirement is mutually and significantly beneficial to both employee and management. The TVA believes that its Take Stock Plan is

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properly a part of its overall employee retirement program and worth every administrative dollar and effort expended. The advantages to the employee are both multiple and significant. They include convenience, dispersion of risk, lower investment cost, and tax benefits. It can safely be assumed that the sense of well being and financial security that consciously and subconsciously builds over the years generates favorable morale and loyalty and enhances the TVA reputation as a progressive, interested employer. More specifically, from the point of view of TVA management, the plan contributes significantly to TVA's manpower management program. It is a recruitment and retention force, and more importantly, it assists in the retirement of aging employees. It reduces management's concern for the moral and morale problems that frequently arise in enforcing retirement age policies (age 65 in TVA). Not infrequently it assists in the early retirement of employees with lagging work motivation. The net result is reduced inefficiency, better morale, and more opportunities for desirable career progression of younger employees.

4. In addition to the above rationale for the Take Stock Plan, TVA appears to have somewhat paternalistic views that management should assist and encourage employees to save and invest wisely in the more profitable, productive, and inflation protected sector of the American economy - common stocks and other equity investments. This is evidenced by the fact that the TVA adopted in 1959 a unique provision in its mandatory employee retirement annuity program. Employees are given the option of having their mandatory retirement contributions placed in either or both of two separate retirement funds. One provides a fixed annuity based on years of service and average salary. The annuities that can be paid have been actuarially determined based on an assumed low 3% interest accrual rate and the monies are invested in high quality fixed-dollar securities that will ensure that retirement liabilities accruing are fully funded. The second fund provides a variable annuity. Contributions purchase proportionate shares in a fund which is invested in both fixed-dollar securities and high quality equity securities. Annuities fluctuate from month to month with the net asset value of the fund but at any period in time, the individual receives the maximum annuity the fund can currently actuarially afford to pay him. In brief, the employee gets the benefit of any high earnings and capital appreciation that the fund may have. This highly audacious and imaginative plan has been so successful that most employees have elected to put all or part of their retirement contributions in the variable annuity fund. At Tab B there are some representative case histories showing the significantly larger annuities that employees in the variable annuity fund are receiving over those they would have received with the same amount of dollars in the fixed annuity fund. In fact, it was the spectacular disparity between the two funds that inspired the Take Stock voluntary retirement plan.

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5. In evaluating the TVA rationale for establishing its Take Stock Plan, it can be pointed out that CIA has far greater reason to be interested in employee preparation for retirement. CIA mandatory retirement age is 60, and earlier retirement is desirable in many cases. This lowering of the normal career span of government employees should itself provide every justification for the administrative effort and expense that would be involved. Further justification lies in the fact that many CIA employees spend substantial periods of their careers overseas performing duties in locations that effectively impair their ability to invest their savings to their best advantage. They are necessarily denied the exposure, information, time, and facilities generally available in the United States for the investment of funds in equity securities. In brief, I personally feel there is ample justification for the CIA to establish a voluntary employee savings and investment mechanism similar to that of the TVA.

6. Possible reasons for not doing so include legal obstacles and possible Congressional or employee criticism in the years ahead concerning the management and the form of the investment plan.

7. Mr.  Assistant General Counsel, is of the opinion that there will be no legal impediments in qualifying a CIA retirement trust to obtain the critical tax exemption benefits. He is also of the opinion that CIA has the authority to expend funds and perform the functions requisite to the operation of the plan.

8. There is the probability that the initiation by CIA of an employee voluntary retirement savings and investment plan will command widespread public attention and interest. It must be assumed that there may well be Congressional or Executive department curiosity, interest, or even concern if only because it may stimulate a desire on the part of other government employees for similar mechanisms. Treasury officials may fear the plan will reduce sales of government bonds and it is important to note that this is the very reason that the TVA requires payroll bond purchase as an eligibility requirement for participation in the Take Stock Plan. In this connection, TVA officials advise me that the plan had no detectable impact upon their sales of government bonds. However, their employee participation in savings bond purchases through payroll deductions had been about 90% before Take Stock was initiated. Since CIA's participation rate is far lower, it seems likely that a similar bond purchase eligibility requirement in the CIA plan would avoid criticism and would actually increase bond purchases by CIA employees.

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9. The most serious risk is employee discontent should the fund perform poorly in a period of recession or should employees become dissatisfied with the management and supervision of the activity. On the first point, TVA officials point out that the risk is minimal. Regular investment over many years without regard to short term market fluctuations is generally acknowledged to be a sound practice for the unskilled conservative investor. Secondly, the retirement fund investor is not really concerned with short term stock market fluctuations; rather he is interested in very long term growth in his retirement savings. TVA officials say that employees are actually pleased with market drops because their contributions purchase more shares in the fund. They appear to understand that their long range interests are a joint function of number of shares acquired and appreciation in share value whether by dividends or capital gains. In addition, they appear to fully appreciate their investment as an inflation hedge.

10. Discontent with the form and rules of the investment mechanism, the particular investment agencies utilized (mutual funds or investment trusts), and the management structure responsible for the operation of the plan is a more serious risk. The TVA has had absolutely no difficulty on this score. I attribute this to the excellent device by which management supervision is provided. The Take Stock Plan is administered by a Board consisting of three representatives elected annually by TVA employees, three representatives appointed by TVA management, and a seventh member selected by the first six. The employee elections are formally conducted with candidates selected from slates prepared by nominating committees consisting of widely respected and known employees. Voting is done by secret written ballot. The three management representatives are senior officers representing the functions of the General Counsel, Personnel, and Finance. The seventh Board member precludes any impasse and assures a bridge between employee and management representatives. This composite Board ensures that TVA employees are directly and effectively represented with regard to the investment of their savings and can promptly and effectively express any dissatisfactions that may arise. At the same time, TVA management is assured that its responsibilities are under proper scrutiny by officials knowledgeable of and responsible for the support services required. As a final control, the Board carries out its planning and supervisory functions under a Trust Agreement between the Board as such and the TVA. The Trust Agreement gives TVA the right of vote over all Board proposals and the right to terminate the Take Stock Plan and distribute the assets to shareholders at any time. It may be that the Trust Agreement was a requisite to approval of the plan by the Internal Revenue Service, but in any event, I would recommend that CIA adopt a similar mechanism as it assumes balanced representation of those most concerned. In addition, I should point out that there is a most effective communications system between

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the Board and the TVA employee body. This is accomplished through numerous meetings of Board members with employee groups and a monthly news letter (Tab C) to all employees which, although informational in text, is highly promotional in effect.

11. Notwithstanding the demonstrated excellence of the TVA Take Stock Plan, I believe CIA could improve thereupon. TVA officials have called attention to numerous ways by which they hope to improve the investment effectiveness of their plan. For example, they are considering shifting their funds to a mutual fund established solely for retirement monies. A fund only concerned with retirement funds would be free from pressure to sell portfolio holdings during a period of market depression to pay off individuals speculating in mutual funds. Such a fund would also be free from pressure to prematurely sell stock with high growth potential in order to demonstrate high capital gains and a high rate of growth during periods of reduced dividends or a depressed stock market merely to appear attractive to new investors. In addition, TVA officials, along with many other investment advisers, believe that smaller mutual funds will generally perform more successfully since they can shift investments with less disruption of the stock market and at lower cost.

12. I also believe CIA can possibly induce the Internal Revenue Service to permit CIA employees to enter the plan with a substantial lump sum investment rather than exclusively by limited payroll deductions. I would argue for this on the basis of the Agency's manpower lump and retirement age policy which gives us a critical need to assist employees to prepare financially for their retirement at an accelerated rate. Similarly, I would argue for a higher permissible rate of payroll deductions as a percentage of gross salary.

13. At Tab D there is a memorandum for the record prepared by Mr. [redacted] containing the views, opinions, and general data that are highly germane to a decision to proceed.

14. It is recommended that the Director of Central Intelligence approve in principle the establishment of a voluntary employee savings and investment retirement plan similar to that of the TVA Take Stock Plan. Such approval is a necessary requisite to the development of a specific proposal since the latter will require extensive negotiations with the Internal Revenue Service and the managers of numerous mutual funds and investment trusts. In addition, it will

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probably be necessary to utilize the services of consultants to obtain the necessary technical and investment expertise. If approval in principle is granted, it is also recommended that a suitable task force be appointed promptly and that appropriate priorities be ascribed to the task. It took the TVA two years to develop its plan. I believe CIA can accomplish this within six months.


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Special Assistant to the  
Deputy Director for Support  
for Special Studies

Atts.

Tab A-D

STATINTL cc: Director of Personnel  
Mr. 

STATINTL SA-DD/S/SS  bak(26 Nov. 68)  
Distribution:

Orig. - Addressee *w/ btl*

1 - ER

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### SPECIFIC PROPOSAL

1. That CIA sponsor the establishment of a voluntary employee savings and investment program as a supplement to the Agency's basic retirement program - the investment of contributed employee funds to be accomplished through a pension trust qualified by the Internal Revenue Service for exemption from Federal income taxes.
2. That the voluntary savings and investment program be administratively supported by CIA as an integral part of Agency personnel and financial operations (payroll deductions, reports to participating employees, administrative and technical direction and supervision).
3. That a task force be established to develop by 30 June 1969 a comprehensive, actionable proposal:
  - a. acceptable to the Internal Revenue Service;
  - b. providing joint CIA employee-CIA management control and supervision of the activity;
  - c. containing specific and alternative recommendations as to the investment media initially deemed most appropriate for the investment and management of the trust funds.

B



**October 1968**

C

Case Histories Based on  
Participation in Variable Annuity Fund

RETIREMENT SYSTEM  
**TVA**  
KNOXVILLE, TENNESSEE 37902

	Retiree Age 65 46.88 units	Retiree Age 63 81.07 units	Survivor Age 61 94.74 units	Retiree Age 65 158.01 units	Retiree Age 60 204.17 units
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Annuity with same  
\$'s in fixed fund

\$52.47	\$94.00	\$101.83	\$186.42	\$245.32
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Variable Annuity:  
Month--Unit Value

Before 1966

25-mo. avg. \$1.223	\$57.33			
17-mo. avg. 1.255		\$101.74		
10-mo. avg. 1.283				
6-mo. avg. 1.288			\$122.03	
1st mo. 1.362				\$215.21

1966

12-mo. avg. 1.313	61.55	106.44	124.39	207.47
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1967

12-mo. avg. 1.444	67.69	117.07	136.80	228.17
3-mo. avg. 1.518				309.93

1968

Jan 1.539	72.15	124.77	145.80	243.18	314.22
Feb 1.437	67.37	116.50	136.14	227.06	293.39
Mar 1.398	65.54	113.34	132.45	220.90	285.43
Apr 1.425	66.80	115.52	135.00	225.16	290.94
May 1.517	71.12	122.98	143.72	239.70	309.73
June 1.580	74.07	128.09	149.69	249.66	322.59
July 1.571	73.65	127.36	148.84	248.23	320.75
Aug 1.516	71.07	122.90	143.63	239.54	309.52
Sep 1.560	73.13	126.47	147.79	246.50	318.51

POST ON BULLETIN BOARDS 10 DAYS

In addition to dollars from variable annuity units, you or your survivor will have income from: (a) TVA's contributions to the Retirement System, (b) contributions the member has in the fixed annuity fund, (c) any monies invested in the TAKE STOCK Plan, and (d) Social Security.

D

Gentlemen:

With the permission and encouragement of the DD/S, I am submitting a specific proposal to you today for your consideration. It is a proposal that I think would contribute significantly to the CIA personnel program and make CIA a leader among government departments and agencies.

My specific proposal is shown on the first page of your "handout."

Each of you has received previously a copy of an analysis I have made of the Tennessee Valley Authority "Take Stock Plan." This Take Stock Plan is the basic inspiration for my proposal. To my knowledge, TVA, through this plan, is the first and only instrument of the Federal government to use a "Qualified Pension Trust" to assist its employees to save and invest personal funds without income tax dilution for their eventual retirement. It is also the first to foster, if not encourage, the investment of such funds in common stocks and other equity securities.

The law of the land provides a tax shelter for limited investment of retirement funds. Private industry and self-employed persons make extensive use of these provisions in retirement planning, so why should not the CIA take the lead in government?

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The basic reasons why I think CIA would be justified in incurring the expense and difficulty of operating a voluntary employee retirement savings and investment plan are enumerated in my paper on TVA activities in this field. I overlooked or underrated the simple reason that the opportunity to do something outstandingly constructive for the benefit of our employees is too great to ignore.

Purposely omitted from your copies of my analysis of the TVA Take Stock Plan are several exhibits which demonstrate the efficacy of investing personal savings for retirement in common stocks through a tax exempt mechanism.

To fully understand these exhibits, it is necessary that I give you a brief description of the total TVA retirement program and its historical evolution.

The TVA normal retirement benefits consist of the following:

- a. Social Security
- b. A pension based on TVA contributions (approximately 6.45% of current payroll) to a pension fund. Pensions are based on years of service and average salary.
- c. An annuity based on mandatory employer contributions at 6% of salary (less social security taxes) to a separate annuity fund.

The combination of all three of these retirement benefit programs roughly equates to Civil Service Retirement.



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Originally the annuity portion of this package provided the retired employee with a fixed monthly payment for life determined actuarially by the amount of money the individual would contribute during his working career and presuming compounded interest at a fixed rate. Initially the rate was 4%, reduced to 3% for new employees during the cheap money depression years, and currently 4% for all employees.

In 1959, however, employees were given the new option of having all or part of their annuity contributions invested in a separate fund which would be invested in common stocks and high yield securities. To the extent this fund appreciated more than 4% per year compounded, eventual annuities would be larger. In the event the fund appreciated at less than 4%, annuities would necessarily be less. In brief, the employee could elect to seek a substantially larger annuity by accepting the risks of receiving a variable annuity.

Are there any questions?

Now for the results - in view of the growth of our national economy and the inflation that has occurred, you will not be surprised. The second page of the handout gives the latest story.

Look first at the box in the lower right-hand corner and the starting date of January 1959. If an individual's contributions had been invested in the fixed 4% fund, contributions of \$100 per month during the past ten years would have grown to \$11,700. The same amount invested in the variable fund would have grown to \$19,892.

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Let me caution you not to be misled by the dollar figures. \$20 to \$50 per month is more realistic than \$100. The important thing is the percentage of growth. In lieu of a fixed 4% growth, the factual record shows an average annual growth of 10.6% for the variable annuity fund. Those who entered this plan in later years have had even more phenomenal growth in their annuity fund. In any event, at the moment it appears that all participants can anticipate substantial increases in their ultimate variable annuity payments.

If you will turn for the moment to the next page, you can see the actual effect upon annuities of several persons who retired between 1959 and 1967 and who were participating in the variable annuity fund.

Case #1 is an employee who elected in 1959 to put his annuity contributions into the variable fund even though he was scheduled to retire four years later. His few years of contributions to the variable fund started him with an annuity of \$57.33. The same money in the fixed annuity fund would have brought \$52.47, almost as much. Yet another four years later, his annuity has increased to \$73.00 per month. This is an increase of 39%. During the same period, no increase has occurred in his TVA pension and increases in social security occur only if enacted by law.

Returning to the prior page, the tabulation in the lower left corner shows how the value of a unit share of the variable annuity has fluctuated with stock market trends. In 1960 and 1962 employees clearly had lost part of their retirement contributions. Nevertheless, the forces of a growing economy and inflation

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This brings me to the last point of my discussion.

The selection of the investment media is clearly of utmost importance. The TVA selection of two mutual funds having the common goal of high growth but by differing investment philosophies permits employees to invest under either or both philosophies. A unique feature of selecting two funds under the same management is that it permits employees to transfer their funds without any penalty from one fund to the other depending upon their personal appraisal of future economic trends.

In any event, the selection of investment media, be they "load" mutual funds, "no load" funds, open or closed end investment companies such as Lehman Brothers, Tri Continental Corporation, trust companies or investment bankers, must be a matter of primary concern to CIA and a matter over which CIA must retain ultimate control. As the materials given you indicate, the TVA has such control.

I am open for questions.

Specific Proposal

1. That CIA sponsor the establishment of a "Voluntary Retirement Trust" as a supplement to its normal retirement program, such trust to be in a form that will qualify under law with the Internal Revenue Service as being exempt from Federal income taxes.
2. That the "Voluntary Retirement Trust" be administratively supported by CIA as an integral part of Agency personnel and financial operations (payroll deductions, reports to participating employees, administrative and technical direction and supervision).
3. That a developmental task force be established to develop a specific proposal acceptable to the Internal Revenue Service, including alternative recommendations as to the investment media seemingly most appropriate for the management of the trust funds.